

**Exhibit B**  
**SEC Decision - File No. 3-10933**

INITIAL DECISION RELEASE NO. 249  
ADMINISTRATIVE PROCEEDING  
FILE NO. 3-10933

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

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In the Matter of	:	
	:	INITIAL DECISION
ERNST & YOUNG LLP	:	April 16, 2004
	:	

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APPEARANCES:                    Stephen M. Sacks, Andrew T. Karron, Randall K. Miller, Robert J. Katerberg, Matthew Laden, and Kathy A. Ladun of Arnold & Porter LLP, and Ralph C. Ferrara and Phillip D. Parker of Debevoise & Plimpton LLP for Ernst & Young LLP

Patricia A. Connell, Associate General Counsel, Ernst & Young LLP

Larry P. Ellsworth, Craig Iscoe, Michael A. Ungar, Jon B. Jordan, J. Lee Buck, II, and Russell G. Ryan for the Securities and Exchange Commission's Division of Enforcement and the Office of the Chief Accountant<sup>1</sup>

BEFORE:                         Brenda P. Murray, Chief Administrative Law Judge

The Securities and Exchange Commission ("Commission") instituted this proceeding on November 13, 2002, pursuant to Section 8A of the Securities Act of 1933 ("Securities Act"), Sections 4C and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), and Rule 102(e) of the Commission's Rules of Practice. The Order Instituting Proceedings ("OIP") charged that Ernst & Young LLP ("EY" or "E&Y"): (1) violated Rule 2-02 of Commission Regulation S-X because it was not independent when it audited the financial statements of PeopleSoft Inc. ("PeopleSoft"), a public company, for fiscal years 1994 through 1999; (2) caused PeopleSoft to violate Sections 7(a) and 10(a) of the Securities Act, Sections 13(a) and 14(a) of the Exchange

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<sup>1</sup> The Initial Decision refers to both the Division of Enforcement and Office of the Chief Accountant collectively as the "Division."

Act, and Exchange Act Rules 13a-1 and 14a-3 thereunder;<sup>2</sup> and (3) engaged in improper professional conduct within the meaning of Section 4C of the Exchange Act and Rule 102(e) of the Commission's Rules of Practice.

Eleven days of public hearings took place in March and April 2003. The Division called fourteen witnesses, including two experts, Douglas R. Carmichael and Walter K. Rush, III, and introduced 844 exhibits.<sup>3</sup> Five Division witnesses were either active or retired EY employees and were represented by EY's counsel. EY called two expert witnesses, Lorin M. Hitt and William A. Mooney, Jr., and introduced 180 exhibits. The record also contains the parties' stipulations ("Stipulations"). The parties' briefs and proposed findings of fact.<sup>4</sup> The final brief was filed on July 21, 2003. Preparation of the Initial Decision was stayed for about a month.

## **I. PRELIMINARY MATTERS**

On July 31, 2003, EY filed a Motion to Supplement the Record with a three-page document and cover letter dated July 30, 2003, from the Executive Director of the Transition Oversight Staff that prepared a Report on the Independence Quality Control Systems of the Four Reviewed Firms ("TOS Report") that is in evidence as EY Ex. 1078. According to the cover letter, the three-page document addresses inaccurate representations that the Division made about the TOS Report in the Division's Reply Brief. The Division filed an opposition contending that the Motion to Supplement the Record does not comply with the Commission's Rules of Practice, and lacks any probative value.

On December 18, 2003, the Division filed a Motion to Supplement the Record. The Division seeks to put into evidence two articles from the November 20, 2003, Wall Street Journal and five documents recently unsealed from state court litigation involving claims that EY and other accounting firms overcharged clients and that EY had potential independence violations due to its relationship with its audit clients. The Division argues that these materials support its request for sanctions. EY opposes the Division's request citing the Commission's Rules of Practice 320, 323, and 326. 17 C.F.R. §§ 201.320, .323, .326. EY also claims the

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<sup>2</sup> The OIP alleges that due to EY's lack of independence, PeopleSoft's annual reports on Form 10-K, for fiscal years 1994 through 2001, as well as its registration statements, prospectuses, and proxy statements filed during that period did not comply with Sections 7(a) and 10(a) of the Securities Act, Sections 13(a) and 14(a) of the Exchange Act, and Exchange Act Rules 13a-1 and 14a-3.

<sup>3</sup> Each hearing transcript volume begins with page one so transcript references are cited by date and page as "(\_\_\_\_, 2003, Tr. \_\_\_\_)." I will refer to the Division's exhibits and Respondent's exhibits as "(Div. Ex. \_\_\_\_)," and "(EY Ex. \_\_\_\_)," respectively.

<sup>4</sup> I will refer to the post hearing filings as follows: Proposed Findings of the SEC's Office of the Chief Accountant and the Division of Enforcement ("Div. Findings of Fact"); Division/OCA's Posthearing Memorandum ("Div. Initial Brief"); Proposed Finding of Fact and Conclusions of Law Submitted by Respondent Ernst & Young LLP ("EY Findings of Fact"); Post-Trial Brief of Respondent Ernst & Young LLP ("EY Brief"); and the Division/OCA's Posthearing Reply Memorandum ("Div. Reply Brief").

Division is wrong to assert that the information portrays EY's current practices, as the materials indicate that the practices at issue ceased by January 2002.

The Commission has made it clear that it favors a liberal standard of admissibility. Del Mar Fin. Serv., Inc., 81 SEC Docket 1691, 1705 (Oct. 24, 2003); City of Anaheim, 71 SEC Docket 191, 193-94 & nn.4-8 (Nov. 16, 1999). Accordingly, I ORDER that the following material is received in evidence:

EY Ex. 1312	July 30, 2003, letter from Jerry D. Sullivan, Executive Director, to the Parties to the TOS Memorandum of Understanding;
Div. Ex. 752	<u>Wall Street Journal</u> , November 20, 2003, article, Ernst Defends Wording Choices;
Div. Ex. 753	<u>Wall Street Journal</u> , November 20, 2003, article, Large Size of Travel Rebates Adds to Questions on Ernst;
Div. Ex. 754	Confidential Travel Management Service Agreement;
Div. Ex. 755	March 20, 1997, letter from Leslie Thompson;
Div. Ex. 756	One-page document dated May 5, 1994;
Div. Ex. 757	One-page document, EY 1997 Preliminary Budget; and
Div. Ex. 758	Multi-page document, Airline Contract Options.

I have given this material little weight because it is difficult to assess its significance without testimony and cross-examination of witnesses familiar with the contents.

Next, I ORDER the Stipulated Corrections To Transcript that the parties submitted jointly on February 18, 2004. 17 C.F.R. § 201.302(c).

## **II. ISSUE**

The issue is whether EY was independent in fact and appearance when it audited PeopleSoft's financial statements for fiscal years 1994 through 1999. Specifically, did EY's business relationships with PeopleSoft, involving EY's Global Expatriate Management System for PeopleSoft and/or actions by EY's consulting group, create an identity or mutuality of interests between EY and PeopleSoft so that EY was not independent in fact and appearance when it issued audit reports on PeopleSoft's financial statements?

### III. FINDINGS OF FACT

My findings are based on the record and my observation of the witnesses' demeanor. I applied preponderance of the evidence as the standard of proof. Steadman v. SEC, 450 U.S. 91 (1981). I have considered all proposed findings, conclusions, and arguments raised by the parties and accept those consistent with this Initial Decision.

#### EY

From at least 1994 until about May 25, 2000, when EY sold its Management Consulting Group ("Consulting"), EY was a "Big Six" accounting firm organized as a limited liability partnership that referred to itself as a leading professional services firm. (EY Findings of Fact at 2) Ernst & Young LLP, SEC No-Action Letter, [2000 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,863 (May 25, 2000). In the period 1996 to 2000, EY had 70,000 to 80,000 employees, annual revenues of \$6 to \$12 billion, and offices in 700 locations in 130 countries. (March 25, 2003, Tr. 96; Div. Exs. 169 at 032052, 413 at 036204, 514 at 040028.) EY's organizational structure was matrix-based, not hierarchical, and it operated on a very decentralized basis. (April 1, 2003, Tr. 123, April 2, 2003, Tr. 84.) The organization consisted of a management committee, a chief executive officer or senior partner, several deputy partners, separate leadership for the practice areas of audit, tax, and consulting, and, at a lower level, regional or area structures. (April 1, 2003, Tr. 127.) EY's national office was spread geographically over EY's twelve regions. (March 25, 2003, Tr. 178.)

EY's audit revenues increased at a much slower pace than revenues from both tax and consulting as shown by figures for two years, 1994 and 1999.

	<u>Audit</u>	<u>Tax</u>	<u>Consulting</u>	<u>Total</u>
1994	\$1,225 million	\$ 543 million	\$ 775 million	\$2,543 million
1999	\$2,205 million	\$1,436 million	\$2,459 million	\$6,100 million

(Stipulations.)

EY was PeopleSoft's auditor from at least 1994 until June 2000, and audited PeopleSoft's financial statements for the year ended December 31, 1994, through the year ended December 31, 1999. (March 25, 2003, Tr. 11; EY Findings of Fact at 3.) EY sold its Consulting practice on or about May 25, 2000, to Cap Gemini Group, S.A. ("Cap Gemini"), and EY was to have no ownership interest in Cap Gemini within five years after the closing. (April 1, 2003, Tr. 9, 15, April 2, 2003, Tr. 66) Ernst & Young LLP, SEC No-Action Letter, [2000 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,863 (May 25, 2000).

#### PeopleSoft

PeopleSoft, founded in 1987 and headquartered in Pleasanton, California, is a leading provider of software applications that assists companies in managing business activities, such as

human resources management systems (“HRMS”), financials, distribution, manufacturing, and supply-chain and higher education.<sup>5</sup> (March 31, 2003, Tr. 8, 201; EY Ex. 1310 at 5-7.) PeopleSoft’s common stock is registered with the Commission and is publicly traded.

As is general industry practice, PeopleSoft’s software is licensed not sold. However, the term sale is used and the licensee is referred to as a purchaser, but it cannot make and resell copies because of the need to protect the creator’s intellectual property. (March 27, 2003, Tr. 200-01, March 28, 2003, Tr. 81-82.) In 1999, PeopleSoft was a leading vendor in integration applications for human resource management, financial management, and enterprise performance analysis. (Div. Ex. 182 at 032253.) Larger business units with at least \$250 million in sales were interested in acquiring PeopleSoft products. (EY Ex. 1310 at 22.) These business firms, including health-care providers, generally retain system integrators (“SIs”) or implementation consultants to, among other things, install, implement, customize, and configure their new sophisticated software programs or significant upgrades.<sup>6</sup> (March 27, 2003, Tr. 203, March 31, 2003, Tr. 9-10; EY Ex. 1310 at 5-6.)

From 1994 through 1996, PeopleSoft was included in Fortune magazine’s list of the fastest growing companies. (Div. Ex. 299, Tab H at 034802.) PeopleSoft’s revenues increased from about \$113 million in 1995 to about \$1.4 billion in 1999. (March 25, 2003, Tr. 18-19.)

### **EY’s Independence Policies on Engagements in Association With Audit Clients**

All EY professionals received a multi-page document effective April 29, 1991, titled “Independence and Related Matters.” It appears that this material is in EY’s Policy and Practice Statement (“PPS”) AA 7502. One paragraph, headed “Engagements in Association with Clients” states:

As provided for in Policy and Practice Statement *Management Consulting Engagement and Client Acceptance* (SCORE Retrieval File No. PP7500), when a proposed cooperative agreement would potentially jeopardize our independence or place us in a potential conflict of interest with an audit client, the regional managing partner, a national director of [Consulting] operations, and the vice chairman of [Consulting] must approve the arrangement before entering into such an alliance. Any cooperative agreement with an SEC audit client is referred to the regional managing partner, the regional director of accounting and auditing, a national director of [Consulting] operations, and the vice chairman of [Consulting] for approval. Cooperative agreements with SEC audit clients may be appropriate in some cases involving separate contracts and separate fee

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<sup>5</sup> One expert described the PeopleSoft system as having two parts: a PeopleSoft platform that acts like an operating system and PeopleSoft modules that provide specific business capabilities. He characterizes PeopleSoft’s products as enterprise software, “applications that are meant to provide a set of capabilities for managing business activities and access to shared data to multiple users in a business.” (EY Ex. 1310 at 5, 7-9.)

<sup>6</sup> In this context, the term “implementation” includes, among other things, installing, configuring, customizing, and consulting on software licensed by third parties. (April 2, 2003, Tr. 187.)

arrangements. However, each situation must be considered on a case-by-case basis.

(EY Ex. 1160 at 003292.) A version marked “1995 draft” sent to Victor Vagar of EY in the Netherlands on February 5, 1996, contains one additional sentence, “Review by the General Counsel’s Office also is required in certain circumstances.”<sup>7</sup> (March 27, 2003, Tr. 49-50; Div. Ex. 134 at 031961) In its brief, EY refers to additional written policies.<sup>8</sup> (EY Brief at 132.)

Each EY employee was ultimately responsible for ensuring that EY observed the rules on auditor independence as to its audit clients, and EY relied heavily on its culture of consultation to assure compliance. (March 25, 2003, Tr. 14, 180-81, March 26, 2003, Tr. 86-87, 90-92, 96-97, 99-100, 115.) “[E]very professional was encouraged to consult with the appropriate people in the firm that had more expertise in the area of independence.” (March 25, 2003, Tr. 45.) Two policies were “at the heart” of EY’s independence system:

1. independence was the responsibility of every professional at E&Y; and
2. because the independence rules were general and depended on facts and circumstances, the firm placed heavy emphasis on the need for every professional – accountant or consultant – to consult with independence experts when questions arose.

(EY Brief at 131.) Edmund Coulson has been EY’s senior person on independence issues in EY’s national office since January 1991, when he left the position of Chief Accountant at the Commission to become a partner in EY’s professional practice group.<sup>9</sup> (March 26, 2003, Tr. 5-6, 9.) Consultations on independence matters are a very heavy focus of Mr. Coulson’s work. (March 26, 2003, Tr. 81.) Unlike his predecessor, Mr. Coulson kept no logs or any other written record of the independence advice that he has provided. (March 26, 2003, Tr. 81.) Mr. Coulson represented that EY considered the necessity of consultation a very important responsibility for

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<sup>7</sup> Mr. Coulson testified that his staff began working on this material in 1994 and put together “do’s” and “don’ts” that were circulated to EY partners. (March 27, 2003, Tr. 49-50.)

<sup>8</sup> EY Ex. 1159, EY Policies and Practice Statement: Management Consulting Engagement and Client Acceptance; EY Ex. 1160, EY Independence and Related Matters: Independence; EY Ex. 1161, EY Policies and Practice Statement: EY Independence and Related Matters; EY Ex. 1162, EY Policies and Practice Statement: Management Consulting Client and Engagement Acceptance; EY Ex. 1163, EY Information Release: Management Consulting Engagement Acceptance Guidelines; and EY Ex. 1164, An Addendum to the Independence Policy and Practice Statement, Independence and Related Matters.

<sup>9</sup> Mr. Coulson received the title “national director of independence” in the late 1990s. (March 26, 2003, Tr. 5-6.) Mr. Coulson holds a bachelor’s degree in accounting from the University of Maryland and is licensed as a certified public accountant in Maryland and New York. (March 27, 2003, Tr. 159-60.) According to Mr. Coulson, he is “considered to be quite reputable amongst the firms, probably the most knowledgeable” on the issue of independence, and the American Institute of Certified Public Accountants recognized his status in 2001. (March 26, 2003, Tr. 84, March 27, 2003, Tr. 158-59.)

every EY employee. (March 26, 2003, Tr. 86-100.) Mr. Coulson knew of only one or two instances where EY fired an employee for failing to consult on an issue of auditor independence. (March 26, 2003, Tr. 101-06.)

In December 1998, John Fridley, a consulting partner who joined EY in 1990 and who was in charge of EY's PeopleSoft Service Line from 1998 to 1999, distributed two pages of informal independence guidance, Relationship Considerations with E&Y Audit Clients and Audit Relationship Guidelines ("Guidelines") to participants at an EY planning meeting. (April 1, 2003, Tr. 136; Div. Ex. 201.) On January 1, 1999, Mr. Fridley circulated the Guidelines to additional people at EY. (March 25, 2003, Tr. 109-11; Div. Ex. 201.) In his investigative testimony, Mr. Fridley stated that he obtained the Guidelines from his predecessor Mr. Lindeman and that Mr. Lindeman did not know who created them.<sup>10</sup> (April 1, 2003, Tr. 133-35.) At the hearing, Mr. Fridley testified that Mr. Lindeman told him the Guidelines came from EY's national office headed by Mr. Coulson. (April 1, 2003, Tr. 134-38.) The Guidelines contained the following prohibitions:

Cannot have a joint marketing program.

Cannot have client and E&Y names appear on a marketing/promotional brochure prepared by either organization.

Cannot jointly host a seminar on a product/service topic. (Can participate on same program with a client without referencing a relationship.)

Cannot make joint calls on multiple prospective clients/customers. (Can respond to individual client/customer request for information.)

Cannot be subcontractor to each other.

Cannot have article(s) published which perceptively endorses/supports either client and/or E&Y services/products.

Cannot have E&Y identified as "preferred" or "partner" or announce that we have an "alliance" or a "relationship."

Cannot take advantage of demo products, education, or technical documentation discounts unless offered broadly to other "Big 6" firms.

Cannot have client reference E&Y services specifically in a client's proposal to a prospective customer.

Cannot participate in any structured Consultant Relations or Partnering program of a client.

Cannot provide to the other organization extensive quantities of the other organization's brochures and other marketing materials for mass mail or trade show distribution to the other party's clients or customers.

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<sup>10</sup> Thomas Lindeman was in charge of EY's PeopleSoft Consulting from 1997 until November 1998. Mr. Fridley was the PeopleSoft Service Line Leader from November 1998, until October-November 1999. (April 1, 2003, Tr. 31, 33.) Lynn E. Anderson, an EY partner, claims that Mr. Fridley also headed the PeopleSoft Service Line from 1995 to 1997, but Mr. Fridley did not mention this in his testimony. (April 2, 2003, Tr. 194.) Mr. Fridley retired from Cap Gemini Ernst & Young in 2002. (April 1, 2003, Tr. 13-14.)



The selection of one party's products or services may not be contingent on the other, and the pricing of one party's products and services cannot be dependent on the other.

CANNOT

Sub/Prime to each other

Submit joint proposals

Refer to E&Y as a "partner," "exclusive," "preferred," or that we have an "alliance" or a "relationship"

Have a joint marketing program, participate in events where the relationship is mentioned, or where E&Y endorses the product

Have the vendor's and E&Y's name or logo appear together on marketing or promotional material

Make joint calls on multiple prospective clients

(Div. Ex. 201.) EY never adopted the Guidelines, which many EY witnesses used as guidance on independence issues. (March 25, 2003, Tr. 116, April 1, 2003, Tr. 52-53, 122.) Much of EY's conduct described in the evidence was contrary to the Guidelines.

Mr. Fridley gave conflicting testimony on procedures that EY had in place so that consulting proposals did not violate the independence standards. Mr. Fridley testified under oath during the investigation that the partner involved was responsible and it was a very decentralized process. (April 2, 2003, Tr. 83-84.) At the hearing, he testified that responsibility was with the engagement partner who had to seek approval from the quality assurance partner, EY legal department, and perhaps the deal review board depending on the size of the proposal. (April 2, 2003, Tr. 82-85.) Mr. Fridley also testified that EY followed procedures described in the document, "Management Consulting Engagement and Client Acceptance," and a question and answer form, and that the number of people who had to approve a consulting contract depended on the nature, size, and risk of the engagement.<sup>11</sup> (April 2, 2003, 100-02, 123; EY Ex. 1159 at 3264.) Mr. Fridley estimated that EY submitted between one hundred and two hundred fifty consulting proposals during the period he headed the PeopleSoft Service Line and he reviewed a half dozen of them. (April 2, 2003, Tr. 103.)

EY audited PeopleSoft's financial statements for the year ended December 31, 1994, through the year ended December 31, 1999. (EY Findings of Fact at 3.) Richard Frick was EY's lead engagement partner on the audits of PeopleSoft's financial statements that were included in Commission filings from 1995 through 2000. Mr. Frick certified that EY was independent, and that each audit was conducted in accordance with Generally Accepted Auditing Standards

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<sup>11</sup> The "Management Consulting Engagement and Client Acceptance," is the SCORE Retrieval File No. PP 7500 referenced previously. It lists certain types of engagements for SEC registrants as a type of consulting engagement that requires additional reviews or approvals than the document specifies and cites Appendix I for details. (EY Ex. 1159 at 003263.) The Appendix states, "Any cooperative agreement with an SEC audit client is referred to the regional managing partner, the regional director of accounting and auditing, a national director of [Consulting] operations, and the vice chairman of [Consulting] for approval." (EY Ex. 1159 at 003269.)

("GAAS"). (March 25, 2003, Tr. 18, 36.) Mr. Frick was also EY's coordinating partner for PeopleSoft from the fall of 1995 until June 2000. (March 25, 2003, Tr. 11.) As the coordinating partner, Mr. Frick was responsible for overseeing all EY services provided to PeopleSoft, and was expected to have a comfort level that all business relationships did not raise independence concerns before signing the audit report.<sup>12</sup> (March 25, 2003, Tr. 36; March 26, 2003, Tr. 113-14.) According to Mr. Frick:

I don't think it was necessary to have these kind[s] of guidelines for people to address independence issues. Our people are educated on independence issues. The firm has extensive policies and procedures that are issued to all employees with respect to independence, and in fact, they have to confirm annually their adherence to the firm's policies and procedures regarding independence.

(March 25, 2003, Tr. 115.) Mr. Frick also testified that the independence rules were pretty vague and not easy to understand. (March 25, 2003, Tr. 44.)

Mr. Mooney<sup>13</sup> opined that:

E&Y established, maintained and monitored independence processes and procedures governing (a) consulting services involving the implementation of computer software developed and sold by its audit clients and (b) the formation of business relationships with audit clients, that were sufficient to provide reasonable assurance that the firm retained its independence from its audit clients and complied with the independence rules and regulations promulgated by the profession and the SEC. . . .

E&Y . . . established an extensive system of controls to educate its partners and staff as to what types of activities were prohibited and what types were of such a nature that they required consultation before proceeding. . . .

The evidence clearly demonstrates that in the case of the subjective arrangements and relationships with PeopleSoft, the system operated effectively. Consultation was initiated when required and the advice given was sound. Furthermore, partners and staff were knowledgeable of what kinds of relationships were prohibited, and they made sure PeopleSoft personnel were also aware of them.

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<sup>12</sup> Mr. Frick was not responsible for overseeing the implementation services that EY provided to third persons. (March 25, 2003, Tr. 11-12.)

<sup>13</sup> Mr. Mooney, a former certified public accountant in Massachusetts, New York, and Connecticut, was a PriceWaterhouseCoopers partner from 1981 to 2001. He was with the predecessor firm of PriceWaterhouseCoopers for thirty-one years, and a firm partner for twenty years. From 1994 until 1998, Mr. Mooney was the senior technical partner for the firm. Mr. Mooney managed PriceWaterhouseCoopers's response to the Commission's investigation of independence in 1998 and 1999. He was the firm's Global Independence Leader in 1999 and 2000, and he was in the Office of the Chairman in 2000 and 2001. (EY Div. 1311, Appendix A.)

(EY Ex. 1311 at 5-6, 26.)

The record does not support Mr. Mooney's opinion. EY relied more on "a culture of consulting" than on written guidelines. (March 25, 2003, Tr. 44-45.) There is no evidence of an extensive system of controls to educate partners; rather, the evidence shows that from 1992 through 1999, EY did not hold any regular training sessions on the subject of auditor independence and that EY's only effort at supervising independence in business relationships with clients was one paragraph in an annual self-reporting form, which was aimed at EY's business relationships with audit clients. (March 27, 2003, Tr. 10-16, April 1, 2003, Tr. 119-20.) There is considerable evidence that EY did not observe the Guidelines. I am unaware that EY submitted any evidence that it followed the directives in "Engagements in Association with Clients," PPS AA 7502, "Management Consulting Engagement and Client Acceptance," PPS 7500, or any other written policy as to its implementation activities with PeopleSoft that the Division has challenged in this proceeding.

### **EY's Business Relationships With PeopleSoft**

In 1996, PeopleSoft described its relationship with EY as four-dimensional:

1. EY's Consulting had an Implementation Partnership with PeopleSoft. From fiscal year 1995 through fiscal year 1999, EY earned approximately \$425 million from implementing PeopleSoft software for third parties.<sup>14</sup>
2. EY's International Tax Group had an Application Software partnership with PeopleSoft for "EY/GEMS for PeopleSoft."
3. EY was PeopleSoft's auditor. EY earned almost \$1.7 million for auditing PeopleSoft's financial statements from 1994 through 1999.<sup>15</sup>
4. EY was a PeopleSoft customer and used PeopleSoft's HRMS Payroll and Financials for its internal operations.

(Div. Exs. 413 at 036205, 185.) EY's business relationships with PeopleSoft concerning software developed by its Tax Group (Number 2 above) and its consulting activities (Number 1 above) are at issue.

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<sup>14</sup> The Stipulations give a total of \$452 million but the sum of the yearly amounts is \$425 million. The yearly fees were \$10 million in 1995, \$40 million in 1996, \$75 million in 1997, and \$150 million in both 1998 and 1999.

<sup>15</sup> The individual totals were \$136,500 in 1994, \$205,000 in 1995, \$155,000 in 1996, \$240,000 in 1997, \$372,000 in 1998, and \$578,000 in 1999.

## **EY's Global Expatriate Management System for PeopleSoft**

EY considered itself the world leader in providing centralized, coordinated expatriate tax return preparation and consulting services. (Div. Ex. 122 at 031907.) In 1976, EY's Tax Group developed an in-house software program for assisting clients with the tax consequences of managing employees with international assignments. (March 21, 2003, Tr. 101-02.) The program had several iterations before EY began offering an Expatriate Tracking System to its customers in 1989. (Div. Ex. 238C at 032792.) In 1990, as the result of "a partnership effort with one of [its] largest clients," EY developed a Global Expatriate Management System ("EY/GEMS"), a DOS-based product. (Id.) In July 1995, EY released EY/GEMS for Windows, followed by EY/GEMS for PeopleSoft in January 1997, and in April 1998, it released EY/GEMS Client/Server ("C/S"). (Id.)

In the early 1990s, EY sought out PeopleSoft for a license to use PeopleTools to develop a new version of EY/GEMS for PeopleSoft. (March 21, 2003, Tr. 123; Div. Ex. 123.) Michael Bishko, a partner and National Director Expatriate Services, initiated the project and led it until he retired on October 1, 1999.<sup>16</sup> (March 21, 2003, Tr. 92, 98-99, 104.) Mr. Bishko believed that an auditor could enter a business arrangement with a client as long as it was a standard industry agreement and not a sweetheart deal, but that the auditor and client could not have joint marketing and sales materials, or joint marketing seminars. (March 21, 2003, Tr. 173.) Mr. Bishko claimed to have told PeopleSoft in late 1993 or early 1994 that EY was required to remain independent from PeopleSoft because it was PeopleSoft's auditor, and that joint marketing efforts, joint sales calls, marketing brochures featuring the PeopleSoft and EY logos, and treating EY differently were all prohibited activities. (March 21, 2003, Tr. 129, 144-46.)

Mr. Bishko claimed that he informed EY's PeopleSoft auditors in the Walnut Creek, California, office and persons in EY's general counsel office that EY was entering a business relationship with PeopleSoft and they voiced no concerns about auditor independence. (March 21, 2003, Tr. 158-59, 281-83.) There are no documents or EY attorneys who can confirm Mr. Bishko's representation, and Mr. Frick, who was located in San Jose, California, was not informed. (March 25, 2003, Tr. 37; Div. Ex. 539.) In 2000, Mr. Bishko did not recall discussing the subject with EY's in-house independence expert, Mr. Coulson. However, in March 2003, after he read Mr. Coulson's investigative testimony, Mr. Bishko recalled that he talked with Mr. Coulson at least three times. (March 21, 2003, Tr. 163-66, 179, March 26, 2003, Tr. 158.)

Based on assurances from Mr. Bishko, Mr. Coulson believed that PeopleSoft routinely issued this type of license and that the arrangement was a license under conditions available to other PeopleSoft customers.<sup>17</sup> (March 26, 2003, Tr. 156-58, 172-73.) Mr. Coulson did not

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<sup>16</sup> Mr. Bishko testified that he relinquished responsibility about a year before he retired, which would have been October 1998; however, an internal EY document generated on April 28, 1999, named Mr. Bishko as head of the project. (Div. Ex. 234 at 032727.)

<sup>17</sup> Mr. Bishko had no first-hand knowledge that the terms and conditions of the Licensing Agreement were standard provisions. Mr. Bishko asked PeopleSoft to draft a standard form agreement and he assumed he got what he requested. (March 21, 2003, Tr. 151.) In fact, the terms and conditions in the few licenses for product development that PeopleSoft issued from

believe that the license created a direct business relationship. (March 26, 2003, Tr. 158-59.) Mr. Coulson reasoned that this was a purchase from an audit client that was not material to the auditor or the client because it was available to other customers under the same conditions.<sup>18</sup> (March 26, 2003, Tr. 161, 172, March 27, 2003, Tr. 150-52.) Mr. Coulson “kept stressing the need to be comfortable that it was the standard kind of arrangement and it is not a sweetheart deal.” (EY Ex. 1311 at 13.) After a few phone conversations, Mr. Coulson advised Mr. Bishko that EY could proceed with the venture without impairing its independence as an auditor. (March 26, 2003, Tr. 158.)

Mr. Bishko for EY and PeopleSoft’s corporate counsel both signed a License and Distribution Agreement for PeopleTools (“Licensing Agreement”), effective October 1, 1994, that terminated in January 1999. (Div. Exs. 121, 465A.) The Licensing Agreement:

A. Allowed EY to use PeopleTools and PeopleSoft HRMS “solely for use in connection with [EY’s] development, Distribution, and provision of technical support for the Derivative Software.”<sup>19</sup> (Div. Ex. 121 at 031894.)

B. Provided that EY would pay PeopleSoft fifteen percent of each license fee it received for the new software, thirty percent of each license renewal fee it received, and a minimum royalty of \$300,000, payable in twelve quarterly payments of \$25,000 each. (Id. at Exhibit A.)

C. Provided that EY would make PeopleSoft a third-party beneficiary of each sublicense. (Id. at 031896.)

D. Provided that PeopleSoft agreed to assist EY’s efforts by providing technical assistance for a \$15,000 quarterly fee [for five quarters]. (Id. at Exhibit A.)

E. Provided that EY shall not distribute the derivative software to PeopleSoft’s direct competitors. (Id. at 031894.)

F. Permitted EY to use PeopleSoft trademarks and tradenames in marketing materials. (Id.)

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1987 to 1993, “were not specifically disclosed.” (EY Ex. 1310 at Tr. 8.) Mr. Bishko did not review any agreements that PeopleSoft had with application partners. (March 21, 2003, Tr. 206-07.) Mr. Bishko heard there were one or two other applications of PeopleSoft HRMS software that had used PeopleTools. (March 21, 2003, Tr. 152.)

<sup>18</sup> Mr. Coulson would reach the same conclusion in 2003. (March 27, 2003, Tr. 146.)

<sup>19</sup> According to one expert, PeopleSoft’s platform was in a “programming language, PeopleCode, which is written or modified using a set of development tools, a product called PeopleTools.” (EY Ex. 1310 at 7.) The Licensing Agreement defines “PeopleTools” as “all or any portion of PeopleSoft’s then current commercially available object code software toolset and associated documentation delivered by PeopleSoft to Licensee hereunder which is designed solely for use in application development and customization of applications.” (Div. Ex. 121 at 031893.)

G. Finally, PeopleSoft maintained a degree of control over the product. EY could not distribute it to certain PeopleSoft competitors. EY had to work with PeopleSoft to establish a reasonable suggested price list, and agreed to work closely with PeopleSoft to ensure the quality of the product. (March 28, 2003, Tr. 92-93; Div. Exs. 121 at 031895, 741 at 10-11, 748 at 5-6, EY Ex. 1310 at 13-15.)

Mr. Bishko was responsible for a January 24, 1995, press release titled “Ernst & Young Announces Licensing Agreement with PeopleSoft to Develop Global Expatriate Management System” that quoted PeopleSoft’s Director of Product Marketing as stating: “EY/GEMS for PeopleSoft will provide a seamless interface of information between PeopleSoft’s software (HRMS) and EY/GEMS, and will allow expatriate human resource managers to access existing employee information from PeopleSoft HRMS, located internationally or at corporate headquarters.” (EY Ex. 122.)

Mr. Bishko’s office submitted a “PeopleSoft Application Partner Profile Questionnaire” to PeopleSoft’s Strategic Marketing Group on March 1, 1995, which listed the target market for the new version of EY/GEMS as “the PeopleSoft market,” and the product as “integrated” with PeopleSoft’s HRMS. (Div. Ex. 600 at 043575-77.) PeopleSoft incorporated information from the questionnaire into an online database for PeopleSoft staff to enable PeopleSoft salespeople in the field immediate access to information about EY’s products and services. “Field representatives will be able to quickly respond to prospects or customers seeking applications like yours which complement the PeopleSoft environment.” (Div. Ex. 600 at 043575.) PeopleSoft’s “Partner Profile” for EY noted under “Red Flags” admonitions very similar to EY’s Guidelines.

E&Y audits PeopleSoft and must maintain an air of independence when dealing with PeopleSoft in the market place. This means that they cannot do joint marketing initiatives, create joint co-logo collateral, subcontract to each other, refer to E&Y as “a partner”, “exclusive”, “preferred” or that we have an alliance. E&Y is a Global Implementation Provider. They are not part of our Global Consulting Alliance program, but have equal capabilities to deliver services globally to our customers.

#### Audit Relationship

As E&Y is the auditor of PeopleSoft, Inc. certain restrictions apply to our relationship. . . .

We cannot:

Submit joint proposals.

Refer to E&Y as a ‘partner’, ‘exclusive’, ‘preferred’, or that we have an ‘alliance’

Have a joint marketing program, participate in events where the relationship is mentioned, or where E&Y endorses the product

Have the [PeopleSoft] and E&Y’s name or logo appear together on marketing material

Make joint calls on multiple prospective customers

(Div. Ex. 169 at 032052.)

In 1999, EY and PeopleSoft engaged in discussions to continue (1) the 1994 Licensing Agreement, and (2) the relationship so as to include upgraded expatriate software in an HRMS/Payroll upgrade. (March 24, 2003, Tr. 14-16, 28-29, 32, 34-35, 37-41; Div. Ex. 237A.) The proposed changes in the PeopleSoft code would eliminate the need for EY to redo coding when PeopleSoft upgraded HRMS. (March 24, 2003, Tr. 35-43.) In communications in the spring of 1999, EY and PeopleSoft discussed how they were going to position the product as PeopleSoft's "preferred solution because of the tight integration and the fact that it was written in the language." (March 24, 2003, Tr. 60-61; Div. Ex. 499E at 039148.) Janice Jane Gonzalez, who worked for PeopleSoft in negotiating with EY, did so at the 1999 PeopleSoft User Conference where she stressed that: EY/GEMS for PeopleSoft was EY's preferred solution; it was written in PeopleTools; and it provided a seamless integration with PeopleSoft software. (March 24, 2003, Tr. 78-79.) On July 19, 1999, EY's Web page had a section that was titled "Managing Your Expatriate Resources Using PeopleSoft and EY/GEMS."

[EY] has worked with PeopleSoft to provide international assignment management functionality needed by many multinational companies utilizing the PeopleSoft HRMS/Payroll System.

EY/GEMS for PeopleSoft gives clients an integrated system solution, incorporating the international assignment capabilities from [EY's] windows version into the PeopleSoft HRMS product using PeopleTools. The design utilizes our in-depth knowledge of expatriate tax, human resources and administrative issues with the most up-to-date technology.

(Div. Ex. 244.) PeopleSoft did not grant these privileges to EY's competitors and agreed to announce the new arrangement at the 1999 PeopleSoft Users Conference. (Div. Ex. 741 at 11.) PeopleSoft announced at the 1999 User Conference that it had found a solution for expatriate processing and that it had a partnership with EY. (March 24, 2003, Tr. 86-90.) Michael Fisher of EY Tax insisted that PeopleSoft inform people at the User Conference that EY/GEMS for PeopleSoft was PeopleSoft's "preferred solution for expatriate software." (March 24, 2003, Tr. 85-91.) Ms. Gonzalez believed that EY and PeopleSoft agreed to do many of the activities that EY's Partner Profile prohibited. (March 24, 2003, Tr. 84-85; Div. Exs. 201, 474.) The negotiations in 1999 did not result in a written agreement.

EY licensed a total of three copies of EY/GEMS for PeopleSoft. (March 28, 2003, Tr. 50.) It granted the last license in September/October 1999.<sup>20</sup> (March 21, 2003, Tr. 260.) EY paid PeopleSoft royalties totaling \$300,000, and technical support and maintenance payments totaling \$75,000, pursuant to the Licensing Agreement.<sup>21</sup> (Stipulations.) EY earned \$767,500 from licensing fees for EY/GEMS for PeopleSoft in fiscal years 1998 through 2001. (Stipulations.)

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<sup>20</sup> The licensees were Applied Materials, Anadarko, and Mobil Oil. The parties and the terms of the 1994 licensing agreement allowed a sale to occur beyond the expiration date of the Licensing Agreement. (March 21, 2003, Tr. 260-61.)

<sup>21</sup> EY made consecutive quarterly royalty payments in 1996, 1997, and 1998, and consecutive quarterly support payments of \$15,000 each beginning in the last quarter of 1994 and continuing

## EY's Consulting Service Implementing PeopleSoft Software

Businesses, including non-profits, often enter into separate contracts with software vendors and implementation consultants.<sup>22</sup> Software implementation can cost two to five times more than the cost of the software, and the implementation process can extend over many months. (April 1, 2003, Tr. 197; EY Ex. 1310 at 7, 20.) According to Dr. Hitt, a “typical” business software application costs approximately \$15 million, and takes, on average, twenty-one months to complete, but installations at large firms with many sites could run into tens of millions.<sup>23</sup> (EY Ex. 1310 at 20.) In the 1990s, there were ten to twenty major SIs that planned software implementations, performed actual implementations, offered training on applications, and redesigned other applications for changed environment. (March 31, 2003, Tr. 196-97, April 1, 2003, Tr. 88-89; EY Ex. 1310 at 21.) In 1998, the implementation or application services market was valued at \$19 billion. (EY Ex. 1109.)

EY's Consulting consisted of Health Care Consulting, Financial Advisory Services, and Consulting. (Div. Ex. 165 at 32039.) In most cases, EY's Consulting assisted clients in selecting software and sometimes assisted with negotiating the contract with the vendor. In other situations, it installed and customized software that the customer had already selected. (April 2, 2003, Tr. 95, 206-08.) EY established a service line for a specific vendor when consulting contracts for a vendor's software reached approximately \$50 million annually. (April 2, 2003, Tr. 188-89.) The mission of EY's Consulting practice was:

to help their clients achieve a competitive advantage by applying technology, improving performance and managing change in a manner that adds value to their organization. Consultants in the [Consulting] practice assist clients with strategic planning, total quality management, business process improvement, cost management, information systems planning, software selection and implementation and reengineering. The [Consulting] practice competes with Andersen Consulting, Price Waterhouse, Deloitte & Touche, Coopers and Lybrand, KPMG Peat Marwick, Computer Sciences Corporation and EDS.

(Div. Ex. 413 at 036204.)

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through 1995. (Stipulations.) EY disclosed to customers that the initial and renewal license fees for EY/GEMS for PeopleSoft included royalties EY paid to PeopleSoft. (March 21, 2003, Tr. 239-41.)

<sup>22</sup> In the 1990s, major software vendors included Arbor Software, Hewlett Packard, Hyperion Software Corp., IBM, Informix, Lotus, Microsoft, Oracle, PeopleSoft, SAP, Texas Instruments, and Xerox Corp. (Div. Ex. 425 at 036532.)

<sup>23</sup> Dr. Hitt received his PhD from the Massachusetts Institute of Technology in 1996. He holds undergraduate and masters degrees in electrical engineering from Brown University. Dr. Hitt is presently the Alberto Vitale Term Associate Professor of Operations and Information Management at the University of Pennsylvania, Wharton School. Dr. Hitt's area of expertise is the management and economics of information systems. (EY Ex. 1310 at 1.) Dr. Hitt provided a detailed description between two types of applications software: personal productivity software and enterprise software, which requires the services of an implementer. (EY Ex. 1310 at 5-6.)



To provide service, an implementation consultant must have a license to use the particular software and associated tools. EY and PeopleSoft entered into an Implementation Partners Agreement (“Implementation Agreement”) on December 15, 1993, that was effective to February 2000.<sup>24</sup> (Div. Exs. 163, 741 at 19.) Mr. Coulson believed that there was consultation in EY on “just about anything that raises any [independence] question about an SEC audit client”; however, there is no evidence that EY consulted with Mr. Coulson and its national office on independence before entering the Implementation Agreement. (March 26, 2003, Tr. 90; Div. Ex. 741 at 23.) The Implementation Agreement:

1. Gave EY a “license, pursuant to PeopleSoft’s standard License Agreement . . . to use the Software to develop Implementation Tools solely in connection with [EY’s] provision of Services to End Users” for one year that envisioned annual renewal;
2. Designated EY as a participant in PeopleSoft’s Implementation Partner Program;
3. Required PeopleSoft to supply its “End Users” and business prospects with a one-page company profile on EY;
4. Gave EY the right to participate in PeopleSoft’s annual User Conference and participate in the product fair;<sup>25</sup>
5. Granted EY technical support and training, and prohibited the disclosure of confidential information; and
6. Specified that EY performed under the agreement as an independent contractor, and that the agreement did not create a partnership, joint venture or agency relationship.

(Div. Ex. 163.) The Division began the investigation that led to this proceeding in 1998 or 1999.<sup>26</sup> Ms. Anderson, and Bill Parsons, PeopleSoft’s Alliance Vice President, signed a Software License Agreement for Global Consulting Companies effective February 17, 2000, that succeeded the Implementation Agreement.<sup>27</sup> (Div. Ex. 277 at 034438, 034442.) There is no

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<sup>24</sup> The original agreement was for one year and it was renewed annually. According to Dr. Hitt, EY exited the business in 2000. (EY Ex. 1310 at 21.)

<sup>25</sup> PeopleSoft held User Conferences in various parts of the world. The one held in the United States was attended by a “huge” number of PeopleSoft customers. (March 24, 2003, Tr. 92.)

<sup>26</sup> In a Wells submission dated June 11, 2001, EY states that the Division’s charges followed a three-year investigation. (Div. Ex. 241 at 032818.) The subject of an “SEC inquiry into PeopleSoft/E&Y Relationship” was an agenda item at a meeting EY held with the new President of PeopleSoft on July 26, 1999. (Div. Ex. 232.)

<sup>27</sup> Ms. Anderson, a consulting partner, replaced Mr. Fridley as head of the PeopleSoft Service Line in October 1999. (April 2, 2003, Tr. 193-94.)

evidence that Ms. Anderson consulted with Mr. Coulson, or anyone else at EY, on independence issues before signing the new agreement.

EY's Web site contained information about the PeopleSoft Service Line and contained a link to the PeopleSoft Web site. (April 1, 2003, Tr. 159.) EY's Auditing Group, Legal Group, Marketing Services Group, and Web Services reviewed material prepared by Ms. Anderson, about EY's services that appeared on PeopleSoft's Web page. (April 2, 2003, Tr. 237.) PeopleSoft's Web site listed EY as an application alliance member and a service alliance partner. (Div. Exs. 724D, 724E.)

By 1997, EY had some 3,600 consultants globally working as implementers in software applications. (EY Ex. 1310 at 26.) By 1998, EY had a PeopleSoft Service Line with 400 consultants and twenty partners located in the United States and over 750 consultants worldwide assigned to PeopleSoft implementations. (March 25, 2003, Tr. 117, April 1, 2003, Tr. 58, 174; Div. Ex. 185.) According to a group that reports on the industry, the Gartner Group, in 1998, EY was rated as the third largest implementer of PeopleSoft globally, and the fourth largest implementer in the United States. (EY Ex. 1310 at 27.) In order of size, EY was rated fifth of the eight largest United States PeopleSoft implementers in 1998. These PeopleSoft consultants were: Andersen Consulting, PeopleSoft, Price Waterhouse, Cambridge Technology Partners, EY, Deloitte & Touche, Hunter, and KPMG Peat Marwick.<sup>28</sup> (EY Ex. 1310 at 21.) Most of EY's consulting proposals were of significant size. (April 2, 2003, Tr. 82.)

EY and PeopleSoft had a symbiotic relationship. (April 1, 2003, Tr. 86-87.) PeopleSoft wanted a lot of consultants capable of implementing its products because as a vendor, PeopleSoft needed fast, knowledgeable implementation to satisfy customers. PeopleSoft believed that EY had direct knowledge of its client accounts that would enable PeopleSoft to differentiate its software to a potential customer. (April 7, 2003, Tr. 47; Div. Exs. 169 at 032054, 306C at 034931.) EY's PeopleSoft Service Line benefited from recommending PeopleSoft products because new PeopleSoft licenses provided more consulting opportunities. A business acquiring software would often ask EY as a consultant to help select a software product, and EY believed it had a better chance of being selected to do the implementation if it had been involved in selecting the software. (April 7, 2003, Tr. 59-61; Div. Ex. 173 at 32131.) EY believed that it was better positioned to be included as a qualified implementer recommended by PeopleSoft if it had a good working relationship with PeopleSoft salespeople. (April 1, 2003, Tr. 220-22.)

PeopleSoft described the fifty to one hundred companies that offered implementation services as service or implementation partners.<sup>29</sup> (March 31, 2003, Tr. 16, 19, 50.) EY's "PeopleSoft relationship was titled an alliance, and the program of implementing PeopleSoft services was called an Alliance program and an Implementation Partner program." (April 2, 2003, Tr. 195.)

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<sup>28</sup> The Gartner Group noted that EY "had a lower overall quality ranking in Gartner's survey than any of the other large external vendors." (EY Ex. 1310 at 27.)

<sup>29</sup> PeopleSoft had hardware partners, software partners, and implementation partners. (April 2, 2003, Tr. 148.)

PeopleSoft had an organization within its corporate marketing department whose job it was to manage PeopleSoft's relationship with its various partners. (April 2, 2003, Tr. 148.) PeopleSoft assigned a "Global Alliance Manager" to EY. One of his responsibilities was to make sure that EY was knowledgeable about PeopleSoft products. (March 31, 2003, Tr. 8.) Documents show EY as a Global Alliance Partner of PeopleSoft, but certain witnesses said EY never formally had this status. (March 31, 2003, Tr. 184; Div. Ex. 490 at 38632.) Stuart Horne, PeopleSoft's Global Alliance Manager for EY from June 1998 to July 1999, believed that PeopleSoft and EY could pursue and close business together as long as "they followed the guidelines and didn't do joint proposals or joint sales meetings." (March 31, 2003, Tr. 7, 74, 153.) Mr. Horne interpreted joint sales calls and joint presentations as occasions when PeopleSoft and EY were present physically together. (March 31, 2003, Tr. 153.) Even though Mr. Horne knew that EY had a different relationship with PeopleSoft than other SIs, Mr. Horne and others generally used the terms "partner" and "alliance member" when discussing EY's relationship with PeopleSoft. (March 31, 2003, Tr. 16, 40-41.) Mr. Horne acknowledged that auditor independence would not allow PeopleSoft to designate EY as its preferred partner. (March 31, 2003, Tr. 185.)

Mr. Fridley saw his role as increasing the business and EY's market share of PeopleSoft implementations. EY's PeopleSoft Service Line had sales of \$150 million and revenue of \$110 million in the United States in fiscal year 1998, and Mr. Fridley projected \$275 million in sales and \$160 million in revenue for fiscal year 1999.<sup>30</sup> (April 1, 2003, Tr. 213-14; Div. Ex. 199 at 032373, 032405.) In December 1998, Mr. Fridley announced that EY needed to have a partner focus on PeopleSoft, and that "I am that partner," and that the business had grown so much that three partners would spend fifty percent of their time "driving business in their area." (Div. Ex. 364 at 035533.)

At the hearing, Mr. Fridley refused to acknowledge that EY and PeopleSoft had a formal alliance, but in a 1999 e-mail, he noted that EY was one of PeopleSoft's twelve alliance partners, he praised Mr. Horne's good work as a Global Alliance Manager, and he argued that EY did not want Mr. Horne "reassigned to another or multiple Partner(s)." (April 1, 2003, Tr. 200; Div. Ex. 226 at 032654.) Mr. Fridley testified that EY could be listed as a member of PeopleSoft's global alliance program, but that EY could not be referred to as a Global Alliance Partner. (April 1, 2003, Tr. 160.) Mr. Fridley testified that EY was one of five companies in PeopleSoft's global alliance program, but he told PeopleSoft not to refer to EY as a Global Alliance Partner because EY did not sign a Global Alliance Partner agreement. (April 1, 2003, Tr. 160-61.) In February 1998, PeopleSoft created a global consulting alliance program with Andersen, Deloitte and Touche, KPMG, and Price Waterhouse as members. (EY Ex. 1310 at 30.)

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<sup>30</sup> One of Mr. Fridley's first engagements at EY was the implementation of PeopleSoft's HRMS software for Bell South from 1992 through 1995. The engagement involved a total of fifty-one EY people but no more than seventeen at any one time and no subcontractors. EY, a co-project manager, earned \$10 million where the client's total implementation cost was over \$100 million. (April 1, 2003, Tr. 23-24.) Mr. Fridley considered the projected growth astronomical considering that the industry was growing at twenty percent, and EY experienced no growth in fiscal year 1999 because of the business downturn. (April 1, 2003, Tr. 218.)

An EY sales document stated, “We have been classified as a PeopleSoft Global Solutions Provider - the highest ranking of a PeopleSoft Implementation Partner – every year since 1991.” (Div. Exs. 425 at 036532, 513 at 39943, 514 at 040032.) Robert Flury, PeopleSoft’s vice president and general manager in 1998, considered EY to be a PeopleSoft global implementation partner since 1991. (March 31, 2003, Tr. 192, 234.) Ms. Anderson considered EY to be a “Global Solutions Provider Partner” like the other Big Six accounting firms. (April 2, 2003, Tr. 238.) Ms. Anderson acknowledged that EY would mention in sales solicitations that it had been a PeopleSoft global implementation partner since 1991 and that it was an alliance member. (April 2, 2003, Tr. 263-64, 273.) Ms. Anderson used the term “implementation partner” because that is what PeopleSoft called the program and it was what customers were familiar with. (April 2, 2003, Tr. 273, 275.) PeopleSoft ranked EY among its top twelve alliance partners. (Div. Ex. 226 at 032654.)

PeopleSoft sent EY draft rules of engagement, “Global Solution Provider Teaming Approach,” in December 1999. The document, which Ms. Anderson believes was sent to all PeopleSoft Global Solution Providers, stated that the “partners” first objective was to maximize revenue for PeopleSoft and its partners. According to the document, “[i]f, during account planning, a partner fails to appropriately commit to heavily influencing a software sale, PeopleSoft may select another partner or use PeopleSoft Consulting in its service strategy for that customer.” (Div. Ex. 359 at 035354.) The rules of engagement also has a diagram that shows joint activities. (Div. Ex. 359 at 035357.) In its response to PeopleSoft, EY did not mention that its status as PeopleSoft’s auditor put limitations on its activities. (April 2, 2003, Tr. 249-52.)

EY’s engaged in a wide variety of actions with PeopleSoft to secure business to implement PeopleSoft software. The Division claims that EY and PeopleSoft’s relationship “involved extensive and intricately interwoven joint activities that created a direct business relationship.” (Div. Initial Brief at 42.) The large amount of evidence can best be understood if grouped into certain subject categories although there is considerable overlap.

### **Joint Sales Efforts**

The evidence is overwhelming that EY partnered with PeopleSoft to the maximum extent possible to accomplish sales and boost EY’s consulting revenues. In 1998, EY earned \$150 million from implementing PeopleSoft software and \$372,000 from auditing PeopleSoft’s financials. In 1999, EY earned \$150 million from implementing PeopleSoft software and \$578,000 from auditing PeopleSoft’s financials. (Stipulations.) The record contains scant mention by EY that sales and marketing activities might be prohibited by EY’s status as PeopleSoft’s auditor. There is no evidence that anyone in EY sought Mr. Coulson’s advice on any independence issue that arose from EY’s consulting activities or that EY complied with the provisions of PPS AA 7502, Engagements in Association with Clients. (EY Ex. 1160 at 003292.)

PeopleSoft sent EY quarterly copies of its “closed business reports,” which indicate the PeopleSoft software sales in which EY was involved. (March 31, 2003, Tr. 67, April 1, 2003, Tr. 104-05; Div. Exs. 311, 319.) From the third quarter of 1997 through the third quarter of

1998, PeopleSoft's closed business reports show that EY was involved in approximately fifty-nine PeopleSoft sales. (Div. Ex. 311.) On six occasions, the report notes that EY provided sales assistance, and on thirty occasions EY is shown as providing help in making the sale, which was rated four or five on a five-point scale, where five is the highest score.<sup>31</sup> (March 31, 2003, Tr. 68-69, 71-73; Div. Ex. 311.) Some comments indicate that EY brought PeopleSoft the lead or initial information that led to the sale, or that EY co-sold with PeopleSoft. (Div. Ex. 311.)

On December 2, 1998, Marie Duginski, PeopleSoft's alliance manager for health care, sent several EY partners information identifying specific PeopleSoft customers in Michigan. (Div. Ex. 291.) In the same communication, Ms. Duginski mentioned the Econosystem concept, which was a concept of Hewlett Packard for a joint project with PeopleSoft and EY, and "opportunities [PeopleSoft] outlined within Henry Ford." (April 7, 2003, Tr. 35-36; Div. Ex. 291.)

On December 1, 1998, Ms. Duginski supplied Mr. Fridley with a confidential closed business report showing customer, product sold, date, the "sales partner" in a column headed "Sales Cycle," a one to five rating for help making the sale, and the system implementer. (March 31, 2003, Tr. 65, 150-51, April 7, 2003, Tr. 20-24; Div. Ex. 292.) EY is shown among the partners. (Div. Ex. 292.) Ms. Duginski's goal was to have more sales by PeopleSoft and EY. (April 7, 2003, Tr. 10-12.) Ms. Duginski urged discretion in how the information was used because she did not want PeopleSoft's other service partners to know that she had disclosed information about them to EY, one of their competitors. (April 7, 2003, Tr. 21-22.)

On June 4, 1999, Mr. Horne informed Mr. Fridley that EY helped close five PeopleSoft sales in the first quarter of fiscal year 1999. (Div. Ex. 319.) PeopleSoft's closed business report for the first quarter of 1998 through the first quarter of 1999 lists forty-six PeopleSoft sales that EY "helped out on." (Div. Ex. 319 at 35075-76.) In half the sales, PeopleSoft rated EY's assistance as either a four or five on a five-point scale. (March 31, 2003, Tr. 145-47; Div. Ex. 319 at 35076.)

In October 1996, five EY partners, including Mr. Frick, met with PeopleSoft executives as part of PeopleSoft's effort to extend its business alliances. As a result of the meeting, the focus of EY's 1997 PeopleSoft practice strategy was to "sustain a 30% practice growth and align with [PeopleSoft] vertically to go after target industries." (Div. Ex. 413 at 036203.) EY's Partner Profile advised PeopleSoft salespeople that:

E&Y has what they refer to as Target Account Leaders. They are senior level partners assigned to cover E&Y's most important clients. These partners generally have a good working relationship with the [chief] level executives and can provide insights on the organization and access to these executives. . . . It is important to identify an E&Y partner within the PeopleSoft service line to help you work with the Target Account leaders and pursuing the customer. . . . When we are in a sales cycle, it can also be helpful to know if E&Y is the audit firm for

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<sup>31</sup> Mr. Fridley claimed that Mr. Horne considered the reports to be of poor quality because they reflect the subjective comments of PeopleSoft's sales personnel. (April 1, 2003, Tr. 97-98.)